

Do not write your name on the assignment. Write your name only on the back of this sheet of paper and staple your answers on the front of this sheet of paper. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to follow these directions will cost you 1 point on the assignment and failure to type it will cost you 10 points.

- 1) (15 points) Explain why a large income tax rate may bring in less tax revenue than a smaller tax rate.
- 2) (15 points) Give an example of the problem with direct offset of expenditures. Do not use the one in the book, nor the one I gave in class. Explain why this is a problem for the economy.
- 3) (25 points) Explain what crowding out is. What is the long-run problem caused by this? Do the long-run consequences depend upon what type of government spending it is? Explain your logic.
- 4) (20 points) When economists want to determine if the government deficit is too large, they calculate the *full-employment budget deficit*. This is what the deficit would be if the unemployment rate was at the natural rate of unemployment. Why do economists not look at the actual budget deficit?
- 5) (25 points) Monetarists feel that fiscal policy should not be done. Unlike the Classical Economists, they feel fiscal policy will affect GDP. However, they feel that it takes so long for the effects to be felt, that the policy should not be done. Explain their logic. A graph may help your explanation.